

VZCZCXRO3606

RR RUEHAG RUEHCHI RUEHDF RUEHFK RUEHHM RUEHIK RUEHKSO RUEHLZ RUEHNAG
RUEHPB RUEHRN RUEHROV
DE RUEHWL #0151/01 1230341
ZNR UUUUU ZZH
R 020341Z MAY 08
FM AMEMBASSY WELLINGTON
TO RUEHC/SECSTATE WASHDC 5212
RUEHRC/USDA FAS WASHDC 0388
RUEHNZ/AMCONSUL AUCKLAND 1661
RUEHDN/AMCONSUL SYDNEY 0670
RUEHBY/AMEMBASSY CANBERRA 5166
RUEHSS/OECD POSTS COLLECTIVE
RUEHZU/ASIAN PACIFIC ECONOMIC COOPERATION
RUCPDO/USDOC WASHDC 0226
RUEATRS/DEPT OF TREASURY WASHDC
RUEHRC/DEPT OF AGRICULTURE WASHDC
RUCNMEM/EU MEMBER STATES COLLECTIVE
RHHMUNA/CDR USPACOM HONOLULU HI

UNCLAS SECTION 01 OF 02 WELLINGTON 000151

SIPDIS

SIPDIS

STATE FOR EEB/TPP/ABT/ATP JANET SPECK AND EAP/ANP
USDA FOR FAS/OFSO JAMES DEVER, FAS/OCRA RALPH BEAN, FAS/OCRA RENEE
SCHWARTZ

E.O. 12958: N/A

TAGS: [EAGR](#) [EAIG](#) [ETRD](#) [ECON](#) [PGOV](#) [PREL](#) [NZ](#)

SUBJECT: IMPACT OF RISING FOOD/AGRICULTURAL COMMODITY PRICES IN NEW
ZEALAND

REF: A) STATE 39410 B) WELLINGTON 115

WELLINGTON 00000151 001.2 OF 002

¶1. Note: This is a joint Foreign Agricultural Service and State
report. Responses are keyed to Ref A questions regarding the impact
of rising food and agricultural prices in New Zealand. End note.

¶2. SUMMARY. As a developed country and a net agricultural
exporter, the recent rise in commodity prices has hit New Zealand
consumers as well as producers that rely on imported animal feed
products. Declining consumer confidence and rising food prices have
been hot topics in New Zealand as food prices have climbed six
percent in the year ending March 2008. The biggest increases in the
grocery food category were for staples -- cheese, fresh milk and
bread -- which are hitting consumers in the pocket book. While
increased grocery prices have translated into higher retail sales,
other sectors are feeling the pinch, especially take-out food sales,
which have fallen six percent from December 2007 to January 2008.
END SUMMARY.

¶3. DEMAND: Soaring food prices are making front page news in New
Zealand. According to the New Zealand Herald, 17 everyday food
items which cost an average of NZ \$134.80 in April last year now
cost NZ \$160.36 - an increase of 28.5%. However, according to
Statistics New Zealand, food prices officially increased 6% in the
statistical year ending March 31, 2008. The most significant upward
contribution came from the grocery food subgroup (up 9%). Within
this subgroup, the most significant upward contributions came from
higher prices for cheese (up 44.2%), fresh milk (up 21.7%), bread
(up 12.2%), and butter (up 82.2%). The inflation rate in New
Zealand is 3.2%.

¶4. Press reports attribute rising food prices to several factors
including increased demand, particularly in China and India where
people are eating more grain, meat, and dairy products as they grow
wealthier. Along with increased demand, news reports also point to:
increased production of biofuels, which has driven up feed costs;
record high oil prices, which make fertilizer as well as the cost of
getting product to market more expensive; climate change including
the drought in Australia, which has driven up the price of wheat in
New Zealand; and governmental policy responses in some of the

hardest-hit nations, which has sometimes resulted in the wrong signals being sent to farmers reducing incentives to grow more food.

15. SUPPLY: While New Zealand consumers are struggling to adjust to higher food prices, high dairy commodity prices have been a boon for New Zealand dairy farmers. The world dairy market is growing at 2 to 3% - enough to take New Zealand's total production. Fonterra, the largest dairy cooperative in New Zealand with a 95% share of the domestic production and a 40% share of world trade in dairy products, hiked its domestic payout to dairy farmers to a record NZ \$7.30 (US\$5.70) per kilogram of milk solids for the 2007/2008 season. This means that Fonterra farmers are likely to receive an average payment of more than NZ \$800,000 (US\$625,000), and NZ \$9 billion (US\$ 7 billion) will be injected into regional economies. The 2006/07 payout was NZ \$4.46 (US\$3.50) per kilogram of milk solids.

16. ECONOMIC IMPACT: In response to higher prices, consumers are reportedly buying fewer dairy products and looking at lower priced alternatives such as milk powder. Others are lobbying for the abolition of sales taxes (GST) on food. The main parties in New Zealand, Labour and National, have resisted previous calls to exempt food from taxes and press reports indicate they are unlikely to change their minds. A spokesman for the opposition National Party indicated the party's first preference would be to tackle the food affordability problem by cutting income taxes. New Zealand is one of only three countries in the OECD that taxes food at the same rate as other goods. Removing GST from all food in New Zealand would reportedly cost the Government about NZ \$2.4 billion (US\$ 1.9 billion) a year.

17. Macroeconomic indicators show New Zealand's annual trade deficit unexpectedly widened in March 2008 as export growth was the weakest in eight months, adding to signs that the economy may have stalled in the first quarter. The shortfall rose to NZ\$4.53 billion (US\$3.6

WELLINGTON 00000151 002.2 OF 002

billion) in the 12 months ending March 31 from NZ\$4.42 billion in the year through February, according to Statistics New Zealand. Overseas shipments, which make up 30 percent of the US\$131 billion economy (GDP), rose at a sixth of the pace economists expected amid falling world commodity prices (Note: Per 2008 IMF Report, prices of non-fuel and non-dairy commodities like meat and agricultural raw materials remain relatively weak reducing returns for producers. End note). Furthermore, a drought has forced some farmers to stop milking cows and send livestock to slaughter. Falling farm production and weaker exports may slow New Zealand's economic growth to a 10-year low in 2008, according to more pessimistic economic estimates.

18. POLITICAL IMPACT: This week Prime Minister Helen Clark said tax cuts to be announced in this year's budget (due to be released May 22) "would deliver timely relief for those families struggling with higher food prices" but she didn't think GST would be removed on food." She further said, "GST had been in place (in NZ) since the mid-1980s when family support schemes like, "Working for Families," began and have now become a more significant form of poverty assistance. PM Clark further said that price increases for items such as butter, cheese and milk, were driven by the export prices farmers were getting for their products. A Labour finance spokesman said a one-off change to GST would not stop international forces pushing up food prices. Other than suggestion of promised tax cuts, the New Zealand Government has not implemented any new policies to address higher food costs. The opposition National Party has not used the rise in food prices as a campaign issue to date but has called for reduction in taxes as way to assist households and stimulate the economy.

19. ENVIRONMENTAL IMPACT: Rising food and agricultural commodity prices have not led to any immediate or significant environmental degradation in New Zealand although, as mentioned above, the effects of the recent drought in Australia and New Zealand have caused the price of some agricultural inputs to rise and were a reason for some New Zealand farmers to send some animals sooner to slaughter.

¶10. POLICY RESPONSE: See ref B for a comprehensive background report on New Zealand's agriculture policy. The government has not made any announcements that it intends to significantly change current policy in the short term in response to rising food prices. However, former Labour Prime Minister and Director-General of the World Trade Organization (1999-2002), Mike Moore has opined that while New Zealand's dairy sector is booming, it has costs other sections of the economy and society. Moore has said that "although dairy products have gone up by more than half for local families, higher prices are good for New Zealand but the implications are complex." He believes New Zealand is suffering from "Dutch disease," which is defined as the deindustrialization of a nation's economy that occurs when the discovery/exploitation of a natural resource (in this case milk) raises the value of that nation's currency, making manufactured goods less competitive with other nations, increasing imports and decreasing exports coupled with the public services more entangled with business interests. Moore's medium to long-term solution to the higher international food prices calls for concluding the WTO's Doha round, which he believes will return four to five times more relief to poverty stricken parts of the world than all the aid and debt forgiveness put together. He also believes that farmers are most productive when they can operate freely with secure property rights. He further sees carefully managed and safe genetically modified (GM) foods as offering great hope for the international food shortages.

¶11. Post will continue to monitor the situation and report on any significant developments.

Keegan